Honduran Exports to U.S. Flat in First Year under CAFTA-DR

A September 2007 report from U.S. Embassy Tegucigalpa

Summary: *One year after entry into force of the Free Trade Agreement between the United States, Central America and the Dominican Republic (CAFTA-DR), Honduran exports to the United States have shown no increase compared with the previous year. Although one year is far too short a period from which to judge, many analysts here are already taking the lackluster performance of the first 12 months as an alarm bell that Honduras needs to get its house in order before it can take advantage of the opportunities presented by the agreement. Others are generally optimistic that benefits will materialize further down the road.*

Optimism Undimmed

According to U.S. Census Bureau foreign trade data, Honduran exports to the United States during the 12 months following entry into force of CAFTA-DR on April 1, 2006, decreased 1.3 percent year on year, to US$ 3.71 billion, compared with US$ 3.76 billion during the 12 months before entry into force.

Despite this performance, the overall enthusiasm for the accord has not diminished. At a spring symposium partly sponsored by USAID, former Trade Minister Norman García of the Foundation for the Investment and Development of Exports (FIDE) noted that with CAFTA-DR, "small exporters can indeed export." García noted that the large number of Hondurans living in the United States (approximately 1 million) represented a significant export opportunity. Rommel Hernandez, the president of *Inversiones Mejia*, a successful oriental vegetables company, said enthusiastically that his company could not even fill all the demand for its products coming from U.S. buyers.

Other sources have provided similarly optimistic assessments to us in private conversations. They noted that with conflicting statistics it is difficult to evaluate CAFTA-DR and that in any case one year is not sufficient to take stock.

Need to Find a Market Niche

There remains, however, widespread recognition that Honduras has some work to do before it can benefit fully from CAFTA. Several analysts cited the need for better market research, better company structure, and a shift in production away from traditional products to those now favored by CAFTA-DR.

A shift away from traditional exports is already beginning to occur. According to the U.S. Census Bureau, Honduran exports of coffee, tea, and spices to the United States fell 13 percent during the 12 months following entry into force of CAFTA-DR, from US$ 66 million to US$ 58 million. Apparel exports were also sluggish, with knit apparel down 2.5 percent from US$ 1.97 billion to US$ 1.92 billion and woven apparel down 9.5 percent from US$ 651 million to US$

589 million. At the same time, however, exports of electrical machinery – including car wiring harnesses – increased 13.8 percent, to US$ 378 million. Exports of precious stones and metals jumped 35 percent to US$ 92 million. And a big winner was sugar, exports of which soared 79 percent from US$ 14 million to US$ 26 million – making the year after CAFTA-DR's implementation the highest on record for Honduran sugar exports.

Knowledge is Power

Many Honduran rural producers lack formal education and understanding of CAFTA-DR. They also often lack the appropriate technology and infrastructure to sell to international markets. Even larger companies may need technical assistance to be able to take advantage of the new export opportunities, according to Embassy sources. "Some companies don't know what they actually need," said one expert.

In addition, some analysts point out that, because of a lack of investment incentives, the vast majority of the remittances that Hondurans living in the United States send back to their relatives in Honduras – which currently amount to about one-fifth of Honduran GDP – are spent on consumption, which boosts imports, rather than invested, which would boost productive capacity and lead to higher exports. Indeed, U.S. exports to Honduras in the first year under CAFTA-DR increased 14.7 percent, from US$ 3.34 billion to US$ 3.83 billion. However, while some of this increase reflected a rise in imports for final consumption – imports of U.S. meat, for example, rose 25 percent to US$ 20 million – there were also strong increases in imports of capital goods and industrial inputs. Imports of cotton, yarn, and fabric increased 20 percent to US$ 508 million; and electrical machinery imports jumped 33 percent to US$ 331 million. Mineral fuels accounted for the largest share of the increase, soaring 60 percent to US$ 517 million (this was probably due mostly to an increase in the prices of petroleum products). Even so, it is undeniable that certain parts of the Honduran population have access to money that could be invested in productive activities given the right incentives.

In addition, some Hondurans complain of the cost and complexity of complying with U.S. hygiene standards for agricultural imports. Honduran agricultural producers need education and training on how to certify their products meet those standards.

Putting Expectations in Perspective

Although most Hondurans greeted CAFTA-DR with enthusiasm and continue to have high hopes that the accord will bring future economic benefits, more sober analysts caution that they should not expect to see huge export gains in the near future. As former Trade Minister García pointed out, beginning in 1984, Honduras enjoyed preferential access to the U.S. market on a non-reciprocal basis under the Caribbean Basin Initiative (CBI). Therefore, before CAFTA-DR entered into force, most Honduran products already entered the U.S. market with low or no import duties, particularly traditional products such as coffee, fruit and textiles. CAFTA-DR removed the uncertainty inherent in the CBI, which required periodic re-authorization by the U.S. Congress. But it did not reduce many duties. For those areas where CAFTA-DR did lower duties or grant new access, Honduras will have to make new investments before it can exploit those opportunities.

Other analysts caution that, even given the trade advantages of CAFTA-DR, Honduras will have difficulty competing in the U.S. market against larger Asian exporters, especially from China and especially in the textile and apparel sector. Honduras has lost market share in that sector to China in recent years. The more pessimistic Honduran analysts believe CAFTA-DR may at best allow Honduras to halt that trend, not reverse it.

Other analysts are less downbeat. According to one Embassy contact, "CAFTA-DR is really only just beginning to see the desired effects."